Filed 3/16/09 Harwood Capital v. Petrominerals CA4/3

NOT TO BE PUBLISHED IN OFFICIAL REPORTS

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

HARWOOD CAPITAL, INCORPORATED,

Plaintiff and Appellant,

v.

PETROMINERALS CORPORATION,

Defendant and Respondent.

G039775

(Super. Ct. No. 00CC06333)

O P I N I O N

Appeal from a judgment of the Superior Court of Orange County, Franz E. Miller, Judge. Affirmed in part, reversed in part, and remanded.

Hornberger & Brewer, Nicholas W. Hornberger, Jason H. Gorowitz and Beverly J. Bickel for Plaintiff and Appellant.

Mazda Butler, Mark N. Mazda and Mark J. Butler for Defendant and Respondent.

* * *

INTRODUCTION

In this, the eighth appeal arising out of the underlying lawsuit, *Sole Energy Company v. Petrominerals Corporation*, Orange County Superior Court case No. 00CC06333,[1] Harwood Capital, Incorporated (Harwood), challenges the judgment entered after the trial court granted the motion of Petrominerals Corporation (Petrominerals) for summary judgment. For reasons we shall explain, we affirm the judgment on Harwood's causes of action for intentional interference with contract and intentional interference with prospective economic advantage, reverse the judgment on the cause of action for fraud, and remand.

Plaintiffs in the underlying lawsuit were Sole Energy Company, a Texas corporation, Sole Energy Company (a limited liability company that was never formed), Thomas R. Swaney, Richard F. Borghese, and Harwood (collectively referred to as Plaintiffs). We refer to Sole Energy Company (the Texas corporation) as Sole Energy Corporation to maintain consistency with prior opinions and to distinguish it from the never-formed limited liability company also called Sole Energy Company, which we will refer to as Sole Energy LLC. Defendants in the underlying lawsuit were Morris V. Hodges, Kaymor Petroleum Products (Kaymor), Hillcrest Beverly Oil Corporation (HBOC), Nevadacor Energy, Inc. (Nevadacor), Petrominerals, and Daniel H. Silverman (collectively referred to as Defendants).

Our decisions in *Sole Energy III*, *Sole Energy V*, and *Sole Energy VII* resolved the underlying lawsuit against all defendants except for Petrominerals. As a

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[1] *Sole Energy Co. v. Petrominerals Corp.* (2005) 128 Cal.App.4th 187 (*Sole Energy I*); *Sole Energy Co. v. Hodges* (2005) 128 Cal.App.4th 199 (*Sole Energy II*); *Sole Energy Co. v. Petrominerals Corp.* (2005) 128 Cal.App.4th 212 (*Sole Energy III*); *Sole Energy Co. v. Petrominerals Corp.* (Apr. 5, 2005, G032255) [nonpub. opn.] (*Sole Energy IV*); *Sole Energy Co. v. Petrominerals Corp.* (Dec. 21, 2006, G036611) [nonpub. opn.] (*Sole Energy V*); *Sole Energy Co. v. Petrominerals Corp.* (Dec. 4, 2008, G039034) [nonpub. opn.] (*Sole Energy VI*); and *Sole Energy Co. v. Hodges* (Dec. 4, 2008, G039197) [nonpub. opn.] (*Sole Energy VII*).

result of our decisions in *Sole Energy III* and *Sole Energy V*, Petrominerals prevailed against all Plaintiffs except Harwood and Sole Energy Corporation. As a result of our decision in *Sole Energy VI*, Sole Energy Corporation's only remaining cause of action is for intentional interference with prospective economic advantage against Petrominerals.

Harwood alleged causes of action against Petrominerals for intentional interference with contract, intentional interference with prospective economic advantage, and fraud. After remand from *Sole Energy III*, Petrominerals moved for summary judgment or summary adjudication against Harwood. The trial court granted the motion, and Harwood's appeal from the resulting judgment is the subject of this appeal. We conclude:

Intentional Interference with Contract and Prospective Economic Advantage. Harwood was not a party to the letter of intent of December 16, 1999, which proposed Sole Energy Corporation would purchase HBOC's stock and oil- and gas-related assets from Nevadacor. Harwood asserts it may recover for interference with contract and prospective economic advantage under the theory it was a third party creditor beneficiary of the letter of intent. Neither the language of the letter of intent nor evidence of the circumstances under which it was made supports Harwood's third party creditor beneficiary theory. Harwood's benefit from the letter of intent and from Sole Energy Corporation's acquisition of HBOC's stock would have been entirely incidental. Harwood therefore cannot recover against Petrominerals for interference with contract and interference with prospective economic advantage.

Fraud. Harwood's fraud cause of action against Petrominerals was derivative of those causes of action against Hodges and Silverman because it was based on alleged misrepresentations they made while acting as Petrominerals's agents or employees. When the liability of a principal is derivative of an agent's, a judgment on the merits in favor of the agent bars recovery from the principal. In *Sole Energy III* and *Sole Energy V*, we affirmed a judgment on the merits in Silverman's favor. Thus,

Harwood cannot recover against Petrominerals for Silverman's alleged fraudulent conduct. In *Sole Energy VII*, we affirmed a judgment in favor of Hodges on a fraud cause of action, but solely on the ground Harwood failed to meet its appellate burden of providing citations to the record and to authority affirmatively demonstrating error on the issues of causation and damages.[2] We exercise our discretion not to give the judgment affirmed by *Sole Energy VII* res judicata effect here because to do so would result in an injustice considering our narrow ground for affirming the judgment in Hodges's favor.

In addition, Harwood produced sufficient evidence to raise triable issues of material fact on each element of fraud. Accordingly, we reverse summary judgment in Petrominerals's favor on the fraud cause of action, but only to the extent that cause of action is based on alleged misrepresentations made by Hodges.

FACTS

I. *The Parties*

Harwood is a California corporation. Swaney is its sole shareholder and president. Borghese is a petroleum engineer and has worked as a technical consultant.

Borghese and Harwood began an informal business partnership in April 1999 and started to use the name Sole Energy Company in about July of that year. Sole Energy Corporation was incorporated in the State of Texas on December 30, 1999. Sole Energy Corporation's shareholders were Harwood and Borghese.

HBOC is a California corporation that owns and operates oil and gas wells in Los Angeles County under long-term leases. Kaymor owns a gas-processing plant abutting HBOC's wells. Hodges is an officer of both HBOC and Kaymor. Nevadacor is a Nevada corporation.

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[2] In response to our invitation, Petrominerals and Harwood each submitted a letter brief addressing two issues: (1) what res judicata effect, if any, did our decision in *Sole Energy VII* have on the judgment that is the subject of this appeal; and (2) whether our decision in *Sole Energy VII* was on the merits for purposes of res judicata.

Petrominerals is a California corporation. Hodges owned shares of Petrominerals and was its president and chief executive officer.

II. *Hodges's Statement That Petrominerals Was Not Interested in Acquiring HBOC*

In May 1999, a broker named Bob Devine approached Swaney and asked him whether he was interested in oil and gas assets in California. Swaney expressed interest, and, in July 1999, Devine introduced Swaney and Borghese to Hodges, who was trying to sell HBOC. On July 2, 1999, Swaney (as president of Harwood) and Hodges signed a confidentiality agreement regarding the potential sale of HBOC's stock. The confidentiality agreement stated that HBOC "is considering the sale of 100% of its issued and outstanding shares of stock to the undersigned."

On July 20, 1999, Borghese and Swaney met with Hodges to discuss the potential sale of HBOC. By then, Borghese and Swaney knew Hodges was the president and chief executive officer of Petrominerals, and a shareholder and officer of HBOC and Kaymor. Borghese was concerned that if Petrominerals were interested in buying HBOC's stock, then, "that would be an unlevel playing field." According to Borghese, at the July 20 meeting, he asked Hodges, "'why isn't Petrominerals doing this HBOC deal?'" Hodges replied, "'it's too expensive and there's a conflict of interest in doing that kind of transaction.'" Borghese was "comfortable" with that answer. According to Swaney, Hodges said there was a conflict of interest and he "couldn't or wouldn't do that." Hodges assured Swaney periodically over the next several months that Petrominerals was not interested in acquiring the stock of HBOC.

Swaney and Borghese would not have pursued the acquisition of HBOC's stock had they been told Petrominerals was interested in the same acquisition.

At the July 20, 1999 meeting, Hodges announced he had hired Daniel Silverman as a consultant to assist in negotiating the sale of HBOC. Soon

thereafter, Borghese met with Silverman and asked him if Petrominerals was interested in acquiring HBOC. Silverman answered, "no, we can't. There's a conflict of interest."

However, in a letter to Hodges dated August 11, 1999, Silverman wrote: "Not to belabor the point with Petrominerals, but I do think that it is possible for P[etrominerals] to purchase [HBOC] if I can go out and bring in some of that mezzanine financing to complete the drilling. . . . Let's talk more maybe next week after we smoke out Harwood and Rich [Borghese]'s abilities." According to HBOC's attorney, Michael Steele, "[t]he interest of Petrominerals in acquiring [HBOC] . . . never ceased."

III. *The Letter of Intent*

On about August 18, 1999, Borghese sent to Hodges by facsimile a nonbinding proposal for discussion purposes to purchase HBOC's assets for $7.5 million. On September 2, 1999, Borghese, on behalf of Sole Energy LLC, signed a proposed letter of intent to purchase HBOC's stock from Nevadacor for $7.5 million. William Herder had signed the proposed letter of intent on Nevadacor's behalf on September 1, 1999.

Sole Energy LLC obtained financing for the transaction in November 1999. In a letter to Hodges, dated November 30, 1999, Borghese stated: "We are prepared to close the purchase of the stock of [HBOC]. [¶] . . . We have financing in place through Bank One as per the term sheet provided."

On December 16, 1999, Borghese submitted a letter of intent to Nevadacor. The letter of intent proposed an entity named Sole Energy Company would purchase HBOC's stock and oil- and gas-related assets from Nevadacor for $7.5 million. The letter was prepared on Sole Energy LLC letterhead stationery, but Borghese signed the letter of intent on behalf of Sole Energy Company. The letter of intent stated: "Except as provided in sections 6 through 11, both inclusive, this letter shall represent a non-binding letter of intent between the parties. This letter of intent shall expire on December 17, 1999, 5:00 CST. Any party may terminate this letter of intent after January 31, 2000,

upon written notice to the other parties, or at any time by all parties with their mutual written consent."

The letter of intent included a provision stating, "[e]xcept as may otherwise be provided in the definitive Stock Purchase Agreement, each of the parties shall be responsible for all costs and expense incurred by such party in connection with this letter of intent, the negotiation and execution of the definitive agreement and the transactions contemplated by this letter of intent and that agreement." The letter of intent included a "no shop" provision and a nondisclosure provision prohibiting the parties from disclosing the existence or terms of the letter of intent to any third party.

On December 23, 1999, Hodges signed the letter of intent on behalf of HBOC and Kaymor. On December 27, 1999, Herder signed the letter of intent on behalf of Nevadacor.

IV. *Termination of Letter of Intent*

On January 7, 2000, attorneys representing Sole Energy LLC submitted a draft stock purchase agreement to HBOC, Nevadacor, and their attorneys. In a letter dated January 20, 2000, Nevadacor's counsel expressed disagreement with or objection to various terms in the draft stock purchase agreement. Other drafts of the stock purchase agreement and correspondence were exchanged.

On February 17, 2000, Bank One provided Borghese and Swaney a financing commitment of up to $6.9 million "to fund the acquisition of the California oil and gas projects we have reviewed and the expansion of your liquids plant."

On February 18, 2000, Borghese telephoned Hodges to discuss limited representations and warranties related to environmental cleanup. Hodges hung up on Borghese during the conversation.

In a letter dated February 25, 2000, Nevadacor and Kaymor terminated the negotiations and the letter of intent without stating reasons.

In March 2000, Petrominerals and Nevadacor entered into a nonbinding letter of intent, prepared by Silverman, to sell HBOC's stock to Petrominerals for $6.7 million and 200,000 shares of Petrominerals's stock. Tony Marino, a representative of Sole Energy Corporation's lender, contacted Borghese to tell him Petrominerals was seeking financing for the acquisition on the same terms as were offered Sole Energy Corporation and was asking for a copy of the environmental impact report on HBOC obtained by Sole Energy Corporation. Borghese told Marino not to give Petrominerals the report. The Petrominerals/Nevadacor transaction was never consummated.

Harwood directly paid Sole Energy Corporation's expenses related to the proposed acquisition of HBOC. Those expenses totaled between $200,000 and $300,000.

PROCEDURAL HISTORY

On May 25, 2000, Sole Energy Corporation filed a verified complaint alleging causes of action for intentional interference with contractual relations, intentional interference with prospective economic advantage, fraud, and breach of contract. Defendants successfully moved for summary judgment on the ground Sole Energy Corporation had not been incorporated when the letter of intent was signed and therefore lacked standing to sue. (*Sole Energy III, supra,* 128 Cal.App.4th at p. 222.)

In September 2001, the trial court granted the motion for summary judgment, ruling that Sole Energy Corporation lacked standing to pursue the litigation. (*Sole Energy I, supra,* 128 Cal.App.4th at p. 191.) Sole Energy Corporation moved for reconsideration of the order granting summary judgment. (*Ibid.*) The trial court deemed the motion for reconsideration to be a motion for a new trial, and granted it. (*Id.* at p. 192.) We affirmed in *Sole Energy I, supra,* 128 Cal.App.4th 187, 198.

Sole Energy Corporation also moved for leave to amend the complaint to add new plaintiffs with standing. (*Sole Energy III, supra,* 128 Cal.App.4th at p. 222.) The trial court granted the motion, and a first amended complaint was filed to add four

new plaintiffs: Sole Energy Partnership, Swaney, Borghese, and Harwood. (*Ibid.*) The trial court stayed the case as to Sole Energy Corporation after Defendants appealed from the order granting the motion for reconsideration. (*Id.* at p. 223.) The case proceeded only on the claims of the newly added plaintiffs—Sole Energy Partnership, Swaney, Borghese, and Harwood—and was tried to a jury on their claims against Petrominerals and Silverman for interference with contractual relations, interference with prospective economic advantage, fraud, and conspiracy. (*Ibid.*) That trial and the posttrial motions were the subjects of *Sole Energy III* and *Sole Energy V*.

On October 27, 2005, Plaintiffs filed a second amended complaint, the operative complaint. The second amended complaint alleged causes of action against Hodges, HBOC, Nevadacor, and Kaymor for breach of contract and fraud, and alleged causes of action against Hodges, Petrominerals, and Silverman for interference with contractual relations, interference with prospective economic advantage, and fraud.

On May 10, 2006, the trial court granted Petrominerals and Silverman's motion for judgment on the pleadings on Sole Energy Corporation's fraud cause of action. On September 29, 2006, an order was entered dismissing Sole Energy Corporation's fraud cause of action with prejudice. Sole Energy Corporation did not challenge dismissal of the fraud cause of action.

Hodges, Kaymor, HBOC, and Nevadacor moved for summary judgment on the ground Sole Energy Corporation lacked standing, and, in the alternative, moved for summary adjudication of the fraud and breach of written contract causes of action. The trial court granted summary judgment. In *Sole Energy VII*, we affirmed, but only on the ground Plaintiffs did not meet their burden as appellants of citing authority or evidence in the record to support the claim of causation and damages.

Petrominerals and Silverman moved for summary judgment against Sole Energy Corporation. The trial court ultimately granted their motions on the ground the

prior judgment affirmed in *Sole Energy III* and *Sole Energy V* barred a subsequent lawsuit under principles of res judicata.

Sole Energy Corporation appealed from the judgment in favor of Petrominerals and Silverman. We granted Sole Energy Corporation's later request to dismiss its appeal as to Silverman. In *Sole Energy VI*, we affirmed the judgment in favor of Petrominerals on Sole Energy Corporation's fraud cause of action, but otherwise reversed the judgment in favor of Petrominerals (with the effect that Sole Energy Corporation has claims pending against Petrominerals for interference with contract and interference with prospective business advantage).

In August 2007, Petrominerals moved for summary judgment against Harwood. The trial court granted the motion. In an order entered December 12, 2007, the trial court stated the fraud cause of action failed as a matter of law "because: (1) it has been finally and fully determined that Harwood's fraud cause of action against Silverman fails, (2) it has been established that Harwood's fraud cause of action against Hodges fails, and that ruling is binding upon this Court at this time, and (3) Harwood's fraud cause of action against Petrominerals is based solely upon the alleged fraud committed by Silverman and Hodges." Judgment was entered on December 13, 2007.

DISCUSSION

I. *Interference with Contract and Prospective Economic Advantage Causes of Action*

Harwood asserted three causes of action against Petrominerals: (1) intentional interference with contract, (2) intentional interference with prospective economic advantage, and (3) fraud. The first cause of action is based on alleged interference with the letter of intent. The second cause of action is based on alleged interference with prospective economic advantage resulting from the letter of intent, that is, Sole Energy Corporation's acquisition of HBOC's stock.

A plaintiff must be a party to an existing contract to recover for interference with contract. (*Blank v. Kirwan* (1985) 39 Cal.3d 311, 330.) To recover for interference with prospective economic advantage, a plaintiff must prove the existence of an economic relationship with a third party that contains a probability of future economic benefit. (*Korea Supply Co. v. Lockheed Martin Corp.* (2003) 29 Cal.4th 1134, 1153.) Harwood was not a party to the letter of intent. Borghese signed the letter of intent on behalf of Sole Energy LLC, and Sole Energy Corporation was to be the entity acquiring HBOC's stock.

Harwood's causes of action for interference with contract and interference with prospective economic advantage are based on the theory Harwood was a third party creditor beneficiary of the letter of intent because it paid for Sole Energy Corporation's expenses incurred in connection with the HBOC transaction, and expected to be repaid and otherwise benefit from Sole Energy Corporation's acquisition of HBOC's stock.

"A creditor beneficiary is a party to whom a promisee owes a preexisting duty which the promisee intends to discharge by means of a promisor's performance. *Wilson v. Anderson* (1962) 208 Cal.App.2d 62 . . . is an illustration. In that case, landowners entered into a contract with broker A to find a buyer for their ranch, but then actually sold the ranch through broker B. Before the sale, the owners and broker B entered into an oral agreement under which B would pay one-third of his commission to A. When B refused to pay A, A sued as a third party beneficiary of the oral agreement between B and the owners. Affirming a judgment for A, the Court of Appeal stated that A was a creditor beneficiary of the oral agreement. The preexisting obligation between A and the owners was the original brokerage contract between them. [Citation.]" (*Souza v. Westlands Water Dist.* (2006) 135 Cal.App.4th 879, 894.)

"'"The test for determining whether a contract was made for the benefit of a third person is whether an intent to benefit a third person appears from the terms of the contract. [Citation.] If the terms of the contract necessarily require the promisor to

confer a benefit on a third person, then the contract, and hence the parties thereto, contemplate a benefit to the third person. The parties are presumed to intend the consequences of a performance of the contract." [Citation.]' [Citation.] A party need not show that it was intended to benefit as an individual and may prevail by showing that it is a member of a class the parties intended to benefit. [Citation.] At the same time, it is not enough that the third party would incidentally have benefited from performance. [Citations.] 'The circumstance that a literal contract interpretation would result in a benefit to the third party is not enough to entitle that party to demand enforcement. The contracting parties must have intended to confer a benefit on the third party.' [Citation.] In determining whether the contract contemplates a benefit to the third party, the court must read the contract in light of the circumstances in which the parties entered into it. [Citation.]" (*Souza v. Westlands Water Dist., supra,* 135 Cal.App.4th at p. 891.)

Whether a party is an intended third person beneficiary of a contract is a question of fact reviewed under the substantial evidence standard. (*Prouty v. Gores Technology Group* (2004) 121 Cal.App.4th 1225, 1233.) But, "where . . . the issue [of whether a third party is an intended beneficiary] can be answered by interpreting the contract as a whole and doing so in light of the uncontradicted evidence of the circumstances and negotiations of the parties in making the contract, the issue becomes one of law that we resolve independently." (*Ibid.*)

An intent to benefit Harwood as a third party beneficiary does not appear from the terms of the letter of intent. It proposed that an entity named Sole Energy Company purchase HBOC's stock and oil- and gas-related assets. The letter of intent does not mention Harwood. Nothing in the letter of intent necessarily required HBOC and Nevadacor to confer a benefit on Harwood, which was to be a shareholder of Sole Energy Corporation. Even if the letter of intent were fully performed, and Sole Energy Corporation acquired HBOC's stock, Harwood's benefit would depend on such factors as

whether Sole Energy Corporation reimbursed Harwood or whether Sole Energy Corporation turned a profit and paid a dividend.

Harwood presented no evidence of a preexisting duty owed to it by Sole Energy Corporation or Sole Energy Partnership which they intended to discharge by means of performing the letter of intent. Although Harwood paid for Sole Energy Corporation's expenses in the transaction, it presented no evidence Sole Energy Corporation obligated itself to reimburse Harwood.

As a putative shareholder of Sole Energy Corporation, Harwood stood to benefit from the acquisition of HBOC's stock. But such benefit would have been purely incidental to consummation of the transaction. "'The circumstance that a literal contract interpretation would result in a benefit to the third party is not enough to entitle that party to demand enforcement.'" (*Souza v. Westlands Water Dist., supra,* 135 Cal.App.4th at p. 891.)

II. *Fraud Cause of Action*

A. *Res Judicata*

Harwood's fraud cause of action was based on alleged representations made by Hodges and Silverman that Petrominerals was not interested in acquiring HBOC's stock due to a conflict of interest. Petrominerals argues, and the trial court found, the judgments in favor of Hodges and Silverman barred Harwood from recovering for fraud. The result of our opinions in *Sole Energy III* and *Sole Energy V* was a judgment on the merits in favor of Silverman on the fraud cause of action. After remand from *Sole Energy III*, the trial court granted the motion of Hodges, HBOC, Kaymor, and Nevadacor for summary judgment against Sole Energy Corporation. In *Sole Energy VII*, we affirmed, but only on the ground Plaintiffs did not meet their burden as appellants of citing authority or evidence in the record to support the claim of causation and damages.

Petrominerals argues res judicata or collateral estoppel bars Harwood's fraud cause of action against it. Under res judicata, a prior judgment bars a subsequent lawsuit on the same cause of action between the parties or their privies. (*Busick v. Workmen's Comp. Appeals Bd.* (1972) 7 Cal.3d 967, 972-973.) Res judicata prevents relitigation of issues that were decided, or could have been litigated, in the prior lawsuit. (*Id.* at p. 975.) Res judicata bars a subsequent lawsuit if three elements are established: (1) the prior lawsuit resulted in a final judgment on the merits; (2) the lawsuit sought to be barred is on the same cause of action as the prior lawsuit; and (3) the party against whom claim preclusion is sought was a party or in privity with a party to the prior lawsuit. (*Id.* at p. 974.)

Collateral estoppel or issue preclusion bars relitigation of issues actually decided in the prior lawsuit. (*Mooney v. Caspari* (2006) 138 Cal.App.4th 704, 717.) Collateral estoppel applies if (1) the issue necessarily decided in the prior lawsuit is identical to the one which is sought to be relitigated; (2) the prior lawsuit resulted in a final judgment on the merits; and (3) the party against whom collateral estoppel is asserted was a party or in privity with a party at the prior lawsuit. (*Ibid.*)

Here, the previous proceedings did produce final judgments in favor of Hodges and Silverman. The judgments were on the same cause of action as in this case—for injuries suffered as a result of alleged fraudulent misrepresentations made by Silverman and Hodges concerning Petrominerals's interest in acquiring HBOC's stock and assets. The party against which Petrominerals asserts res judicata and collateral estoppel—Harwood—also was a party to the judgment in Silverman's favor affirmed in *Sole Energy III* and *Sole Energy V*, and to the judgment in favor of Hodges, HBOC, Kaymor, and Nevadacor affirmed in *Sole Energy VII*.

When the liability of a principal is derivative of an agent's, a judgment on the merits in favor of the agent bars recovery from the principal. (*Brinton v. Bankers Pension Services, Inc.* (1999) 76 Cal.App.4th 550, 557-558; see also *Richard B. LeVine,*

Inc. v. Higashi (2005) 131 Cal.App.4th 566, 576-578; *Plott v. York* (1939) 33 Cal.App.2d 460, 464.) Harwood's fraud cause of action against Petrominerals was based entirely on the same alleged fraudulent conduct that served as the basis for the fraud causes of action against Silverman and Hodges individually. Harwood alleged Petrominerals's liability was derivative of that of Silverman and Hodges, who acted in the course and scope of their agency or employment with Petrominerals when the alleged misrepresentations were made.

Thus, the judgment affirmed in *Sole Energy III* and *Sole Energy V* bars Harwood's fraud claim against Petrominerals to the extent it is based on liability derivative of Silverman. As to Hodges, we affirmed a judgment in his favor in *Sole Energy VII*, but only on the ground Plaintiffs failed to meet their burden as appellants of citing authority or evidence in the record to support the claim of causation and damages. We concluded: "Plaintiffs have failed to meet their appellate burden of affirmatively demonstrating error on the issues of causation and damages. Since damage resulting from the fraud is an essential element of a fraud cause of action [citation], we affirm summary judgment on the fraud cause of action." (*Sole Energy VII, supra,* G039197.)

Was our affirmance in *Sole Energy VII* on the merits, as required for res judicata? Or did we affirm for technical reasons unrelated to the merits?

The requirement of a final judgment on the merits "is derived from the fundamental policy of the doctrine, which gives stability to judgments after the parties have had a fair opportunity to litigate their claims and defenses." (7 Witkin, Cal. Procedure (5th ed. 2008) Judgment, § 370, p. 994.) A judgment not on the merits does not operate as a bar under res judicata. (*Goddard v. Security Title Ins. & Guar. Co.* (1939) 14 Cal.2d 47, 52.) For example, a judgment resulting from an order sustaining a special demurrer for technical or formal defects is not on the merits. (*Ibid*.)

Res judicata or collateral estoppel will not be applied, even if its threshold requirements are met, "if injustice would result or if the public interest requires that

relitigation not be foreclosed. [Citations.]" (*Consumers Lobby Against Monopolies v. Public Utilities Com.* (1979) 25 Cal.3d 891, 902; *Mooney v. Caspari, supra,* 138 Cal.App.4th at pp. 717-718; see *Citizens for Open Access etc. Tide, Inc. v. Seadrift Assn.* (1998) 60 Cal.App.4th 1053.)

We conclude an injustice would result here from applying the judgment affirmed by *Sole Energy VII* as res judicata or as collateral estoppel against Harwood's fraud cause of action against Petrominerals. In reaching this conclusion, we examine our opinion in *Sole Energy VII* and consider the basis on which we affirmed. (See 7 Witkin, *supra,* Judgment, § 370, p. 995 ["It is often necessary to examine the record of the proceedings to determine whether a particular adjudication is to be considered res judicata"].) In *Newport Beach Country Club, Inc. v. Founding Members of Newport Beach Country Club* (2006) 140 Cal.App.4th 1120, 1123, we held: "[W]hen a trial court judgment decides a case on two alternate grounds, and the appellate court affirms based on one ground, the judgment is binding under principles of res judicata and collateral estoppel only on the ground addressed by the appellate court." While this case presents a different situation than in *Newport Beach Country Club, Inc. v. Founding Members of Newport Beach Country Club,* that case teaches we can consider the basis on which we affirmed in determining the res judicata effect of the judgment.

In *Sole Energy VII,* we did not conclude Harwood did not or could not prove causation and damages; we concluded only that Plaintiffs failed to cite to authority and evidence in the record to meet their burden as appellants. Nor did we resolve any other issue on the merits. In this case, as we explain later, Harwood did meet its appellate burden, and has cited evidence establishing at least a triable issue as to whether it suffered damages proximately caused by Petrominerals's alleged misrepresentations. As we will explain too, those damages are precisely the type of damages we recognized in *Sole Energy III* to be recoverable by a shareholder individually.

Declining to give res judicata or collateral estoppel effect to the judgment affirmed by *Sole Energy VII* would not undermine the policies of giving stability to judgments and preventing inconsistent judgments because our opinion fully explains the limited basis of our affirmance. Our decision here does not question or lessen the validity of that judgment, but, by considering our reasons for affirming the judgment, accords it its proper weight and value.

B. *Triable Issues as to Elements of Fraud*

The elements of a cause of action for fraud are (1) misrepresentation of fact, (2) knowledge of falsity, (3) intent to defraud, (4) justifiable reliance, and (5) resulting damage. (*Small v. Fritz Companies, Inc.* (2003) 30 Cal.4th 167, 173.) Petrominerals argues Harwood failed to raise a triable issue of fact on the elements of misrepresentation of fact, justifiable reliance, and damages. We disagree.

1. Justifiable Reliance

Petrominerals argues the July 2, 1999 confidentiality agreement demonstrates Harwood could not have justifiably relied on Hodges's representations. The relevant part of the confidentiality agreement states: "BUYER [Harwood] understands and acknowledges that neither COMPANY [HBOC] nor COMPANY'S affiliates nor any of the employees, officers, directors, agents or other representatives of COMPANY or COMPANY's affiliates make any representation or warranty as to the accuracy or completeness of any information provided by COMPANY to BUYER, except as may be set forth in a definitive written purchase and sale agreement. Furthermore, except as may be expressly provided in a definitive written purchase and sale agreement related to the HBOC stock, BUYER covenants not to sue COMPANY and affiliated companies, and employees, agents and other representatives of COMPANY and COMPANY's affiliates for any claim or action that may arise out of or may be incident to BUYER's use of information provided to BUYER."

Hodges was both an officer of HBOC and an officer of Petrominerals. Harwood alleged Hodges was acting as a representative or agent of Petrominerals when he told Borghese and Swaney that Petrominerals was not interested in acquiring HBOC. The confidentiality agreement, which applied to HBOC and its representatives, therefore would not apply to representations made by Hodges on behalf of Petrominerals.

Petrominerals also argues Harwood could not have justifiably relied on Hodges's representations because the letter of intent was expressly nonbinding. Petrominerals was not a party to the letter of intent, and, as we concluded earlier, was not a third party beneficiary of it.

However, portions of the letter of intent were binding, and the binding portions raised a triable issue of fact as to whether Harwood's continued reliance on Hodges's representations was justified. Section 12 of the letter of intent states, "[e]xcept as provided in sections 6 through 11, both inclusive, this letter shall represent a non-binding letter of intent between the parties." Section 6 (the no shop provision) of the letter of intent provides in part, "[u]pon your execution of this letter of intent until the last to occur of the termination of this letter of intent or January 31, 2000, HBOC, Kaymor, and [Nevadacor] agree that they shall not directly or indirectly (a) solicit, (b) encourage the submission of offers or proposals from any person or entity with respect to, (c) initiate or participate in any negotiations or discussions regarding, or (d) enter into (or authorize) any agreement or agreement in principle with respect to, any expression of interest, offer, proposal to acquire or acquisition of either all or a substantial portion of HBOC's business or assets or any of its capital stock." Section 8 of the letter of intent provides that no party will disclose to any third party "any information regarding the existence of this letter of intent, the terms of the proposed transaction, or the existence of or status of negotiations with respect to the proposed acquisition" at any time before "execution and delivery of a definitive Stock Purchase Agreement."

Sections 6 and 8 of the letter of intent were binding and raised at least a triable issue of fact as to whether it was justifiable for Harwood to continue to rely on Hodges's representation that Petrominerals was not interested in acquiring HBOC.

2. Falsity

Petrominerals contends Hodges's statement that Petrominerals was not interested in acquiring HBOC was not actionable as fraud because it was an expression of opinion or a prediction of a future event, not a representation of fact. We conclude there is a triable issue of fact whether Hodges made a statement of fact.

An action for fraud must be based on a statement of fact, and cannot be based on an expression of opinion or a prediction of future actions by third parties. (*San Francisco Design Center Associates v. Portman Companies* (1995) 41 Cal.App.4th 29, 43-44; see also 5 Witkin, Summary of Cal. Law (10th ed. 2005) Torts, § 774, pp. 1123-1124.) "A representation is one of opinion if it expresses only [¶] (a) the belief of the maker, without certainty, as to the existence of a fact; or [¶] (b) his judgment as to quality, value, authenticity, or other matters of judgment." (Rest.2d Torts, § 538A.)

Taking a page from defamation law, we conclude a totality of the circumstances test should be used to determine whether a statement is actionable. (*Franklin v. Dynamic Details, Inc.* (2004) 116 Cal.App.4th 375, 385.) Under the totality of the circumstances test, we consider the language of the statement and the context in which it was made. (*Id.* at pp. 385-386.)

According to both Borghese and Swaney, Hodges made three affirmative representations: (1) Petrominerals was not going to try to purchase HBOC because (2) it was too expensive and (3) there would be a conflict of interest. Hodges did not couch those representations with expressions of belief or opinion. Each representation could be shown to be objectively true or false at the time it was made. The representations arose during initial discussions between Borghese and Hodges about the sale of HBOC. Borghese was concerned because he knew Hodges was president and chief executive

officer of Petrominerals and it was pursuing oil and gas acquisitions. Borghese was not eliciting opinion—he wanted assurance his efforts in trying to acquire HBOC would not be wasted. Borghese testified he was "comfortable" with Hodges's answer.

Hodges's statement does not appear necessarily to be a prediction of future action by a third party for two reasons. First, Hodges could be making a representation that Petrominerals at that time was not interested in purchasing HBOC. Second, Petrominerals was not a third party because Hodges was its president and chief executive officer. Hodges would know as a fact whether Petrominerals intended to pursue the acquisition of HBOC and, if not, why. We therefore conclude, under the totality of the circumstances, there is a triable issue of fact as to whether Hodges made representations of fact or expressed opinions.

3. Materiality of Misrepresentation

Petrominerals argues Hodges's misrepresentations of fact were not material because they were made several months before the parties entered into the letter of intent. We conclude the evidence was sufficient to raise a triable issue of fact on materiality.

The evidence showed Borghese and Swaney wanted assurances that Petrominerals would not be interested in acquiring HBOC before they proceeded with negotiations and expended due diligence money. Borghese testified at the trial in *Sole Energy III*, "[m]y concern was that if Petrominerals was interested in buying HBOC, that that would be an unlevel playing field. [¶] I might add, it's as bad as playing poker against somebody and the guy you're playing against has a friend looking at your cards telling the guy you're playing against what your hand is. Very uneven, unfair." Borghese testified he would have done nothing further to acquire HBOC if he had been told Petrominerals was also interested in acquiring it. Nonetheless, Hodges assured Swaney periodically over the next several months that Petrominerals was not interested in acquiring the stock of HBOC.

4. Damages

Petrominerals argues Harwood cannot prove damages because section 11 of the letter of intent provides that each party shall be responsible for its own costs and expenses incurred in the transaction. However, neither Harwood nor Petrominerals was a party to the letter of intent. Harwood is not seeking to recover expenses incurred under the letter of intent, but is seeking fraud damages from Petrominerals. Those fraud damages are not unrecoverable breach of contract damages just because they happen to be the costs and expenses incurred in connection with the HBOC transaction.

In this case, in stark contrast to *Sole Energy VII*, Harwood does cite to evidence in the record that it paid for all of Sole Energy Corporation's expenses and costs of due diligence incurred in the attempted purchase of HBOC. In *Sole Energy III*, we noted a putative shareholder of a corporation could recover those very types of damages. While concluding in *Sole Energy III* a putative shareholder may not recover the corporation's lost profits in a nonderivative suit, we recognized the shareholder may recover individual damages. We discussed *Sutter v. General Petroleum Corp.* (1946) 28 Cal.2d 525 (*Sutter*) and *Nathanson v. Murphy* (1955) 132 Cal.App.2d 363 (*Nathanson*), and, with respect to the latter case, stated: "Describing *Sutter* as similar, the [*Nathanson*] court held the plaintiff could recover damages because the misrepresentation was made directly to Nathanson, before the corporation was formed, to induce him to make the $5,000 down payment. (*Nathanson, supra,* 132 Cal.App.2d at p. 370.) Although Nathanson made the down payment on behalf of the corporation formed to acquire the ranch, Nathanson could sue for individual recovery because the down payment constituted an investment in the corporation and Nathanson was injured when he lost that investment as a consequence of Murphy's fraud. (*Id.* at pp. 370-372.)" (*Sole Energy III, supra,* 128 Cal.App.4th at p. 231.)

We explained why *Sutter* and *Nathanson* precluded Swaney and Borghese's recovery of Sole Energy Corporation's lost profits: "[A]s in *Sutter* and

Nathanson, Plaintiffs in this case contend they were injured by wrongs directed to them individually and occurring before Sole Energy Corporation was formed. *Sutter* and *Nathanson* upheld recovery of the amount of the plaintiffs' respective lost investments because in each case the plaintiff individually suffered injury as the proximate result of the defendants' tortious conduct. Those injuries included loss of investment in the later-formed corporation. But neither *Sutter* nor *Nathanson* addresses the issue presented here: Whether the putative shareholders can recover their proportionate shares of the corporation's future lost profits. [¶] We conclude Borghese and Swaney, as putative shareholders of Sole Energy Corporation, could not recover their proportionate shares of the corporation's lost profits. Neither *Sutter* nor *Nathanson* alters the long-established proposition that a shareholder does not have an ownership interest in corporate profits. *Sutter* and *Nathanson* are reconcilable with *Nelson*[*v. Anderson* (1999) 72 Cal.App.4th 111], for a shareholder's out-of-pocket investment in the corporation is not the same as lost future corporate profits." (*Sole Energy III, supra,* 128 Cal.App.4th at p. 232.)

We also stated, "*Sutter* based its conclusion on the proposition a shareholder may recover damages for injuries the shareholder individually suffered as a proximate result of tortious conduct directed to the shareholder." (*Sole Energy III, supra,* 128 Cal.App.4th at p. 232.) In this case, Harwood, as the plaintiff in *Nathanson*, sued to recover for injuries it suffered individually as a proximate result of Petrominerals's fraudulent conduct directed to Harwood. Those injuries consist of Harwood's out-of-pocket expenses incurred in the attempted acquisition of HBOC stock. If proven, Harwood may recover damages for those injuries.

5. Assignment

Finally, Petrominerals argues Harwood assigned its rights under the letter of intent to Sole Energy Corporation when it was incorporated on December 30, 1999. Harwood's fraud cause of action does not assert rights under the letter of intent, but seeks damages independent of it based on Hodges's misrepresentations.

DISPOSITION

The judgment in favor of Petrominerals is affirmed on Harwood's causes of action for intentional interference with contract and intentional interference with prospective economic advantage. The judgment is reversed as to the fraud cause of action but only to the extent that cause of action is based on alleged misrepresentations made by Hodges. The matter is remanded for further proceedings. In the interest of justice, no party shall recover costs incurred in this appeal.

FYBEL, J.

WE CONCUR:

SILLS, P. J.

ARONSON, J.